No. 10,697

United States Circuit Court of Appeals

For the Ninth Circuit

AMELIA DAVIS BLOCH,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Upon Petition to Review a Decision of the Tax Court of the United States

PETITIONER'S REPLY BRIEF

W. H. ORRICK,
CHARLES L. BARNARD,
Financial Center Building,
San Francisco, Calif.
Attorneys for Petitioner

ORRICK, DAHLQUIST, NEFF,
BROWN & HERRINGTON,
Financial Center Building,
San Francisco, Calif.
Of Counsel

PARKER PRINTING COMPANY, 545 SANSOME STREET, SAN FRANCISCO

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I.

RE STATEMENT OF QUESTION INVOLVED

Petitioner in March, 1940 sold 212 common shares of The Dow Chemical Company (hereinafter called Dow) which she had acquired in exchange for preferred and common shares of Great Western Electro-Chemical Company (hereinafter called Great Western) in connection with the statutory merger of Great Western with and into Dow. Petitioner contends that the basis of such Dow shares is to be determined by reference to the specific Great Western shares for which they were exchanged. Respondent contends that the basis of the Dow shares sold is

to be determined by dividing the aggregate cost of all Great Western shares held by Petitioner immediately prior to the effective date of the statutory merger by the number of Dow shares acquired by her on the statutory merger and multiplying the result that is obtained by 212, the number of shares sold. (For convenience this method shall be referred to by the name given to it by Respondent, viz: the "average cost rule" [Resp's. Br. p. 10].)

It is conceded by both parties that the statutory merger was a "reorganization" under Section 112(g)(1), the exchange of the Great Western shares for Dow shares is "tax free" under Section 112(b)(3), and the basis of the Dow shares acquired on the statutory merger—and, consequently, the determination of the question here presented—is governed by the provisions of Section 113(a)(6) (Op. Br. pp. 9-11; Resp's. Br. pp. 9-16).

It is established by the decisions and admitted by Respondent (Resp's. Br. pp. 15, 27) that under Section 113(a)(6) the basis of shares of a corporation acquired in a "reorganization" in exchange for shares of the same corporation is the same as the basis of the specific shares for which they were exchanged.

> *Fuller v. Commissioner* (C.C.A. 1st, 1936) 81 Fed.(2d) 176.
>
> See, also, *Kraus v. Commissioner* (C.C.A. 2d, 1937) 88 Fed.(2d) 616.

Respondent seeks to distinguish the rule of the *Fuller* and *Kraus* cases on the ground that the instant case involved the exchange of stock of *one* corporation for stock of *another* corporation and, in support of this distinction, relies upon the decision of the United States Board of Tax Appeals in *Fleischmann v. Commissioner* (40 B.T.A. 672).*

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*Respondent also cites the decision of the Third Circuit Court of Appeals in *Arrott v. Commissioner* (C.C.A. 3d, 1943) 136 Fed.(2d) 449. However, the language quoted is dictum, since no identification between the shares acquired and the shares surrendered was established. This point is conceded by Respondent (Resp's. Br. p. 19).

Petitioner in her Opening Brief relied on two alternative grounds.

First: The instant case is governed by the rule of the *Fuller* and *Kraus* cases and not by the rule of the *Fleischmann* case. In the *Fleischmann* case—which involved the basis of stock of the transferee corporation acquired in exchange for stock of the transferor corporation on a reorganization involving a transfer of assets by the transferor to the transferee—there was no identity between the shares of the transferor corporation and the shares of the transferee corporation, nor between the transferor corporation and the transferee corporation. In the instant case —which involves a statutory merger—such identity between the Great Western and Dow shares and between Great Western and Dow is established by law (Op. Br. pp. 11-24).

Second: The rule of the *Fleischmann* case is wrong; there being no justification under Section 113(a)(6) for a distinction —sanctioned by the *Fleischmann* case—in the manner of determination of the basis of stock of a corporation acquired on a "reorganization" depending on whether received in exchange for (i) stock of the same corporation, or (ii) stock of another corporation (Op. Br. pp. 25-28).

Petitioner in this brief will first discuss Respondent's argument on the First ground and then Respondent's argument on the Second ground.

II.

RESPONDENT IS MISTAKEN IN HIS CONTENTION THAT A STATUTORY MERGER IS NOT DISTINGUISHABLE IN LEGAL EFFECT FROM A REORGANIZATION INVOLVING A TRANSFER BY ONE CORPORATION OF ITS ASSETS TO ANOTHER CORPORATION AND THE ISSUANCE BY THE TRANSFEROR CORPORATION OF ITS STOCK IN EXCHANGE FOR THE STOCK OF THE TRANSFEREE CORPORATION.

Respondent takes the position that an exchange of stock on a statutory merger is not distinguishable from an exchange of stock of a transferor corporation for stock of a transferee corporation in connection with a "reorganization" in which the transferee transfers its assets to the transferor and, in support of his position, argues:

(a) The Great Western shares were not individually exchanged for Dow shares, either by (i) operation of law, or (ii) the Merger Agreement (Resp's. Br. pp. 16-17 and footnote 7).

(b) The Federal Courts in applying the Federal Tax statute should disregard any provision of local law providing for such individual exchange in order "to give the statute uniform application" (Resp's. Br. p. 16, footnote 7).

(c) The first exchange and the second exchange referred to in Petitioner's Opening Brief (Op. Br. pp. 11-13) are one integral transaction which was not consummated until the issuance of the Dow certificates. The Great Western certificates, from and after the effective date of the merger, did not represent any interest in Dow (Resp's. Br. p. 17, footnote 8).

(d) There is no identity between the Great Western shares and the Dow shares, since the respective interests represented thereby are different. It is impossible to identify any individual Great Western share with the Dow share into which it is converted (Resp's. Br. pp. 25-27).*

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*Respondent also at some length (Resp's. Br. p. 14) discusses an argument, imputed to Petitioner, that, since the instant exchange was an involuntary exchange, the rule of the *Arrott* case, *supra,* is not appli-

Respondent does not take issue with Petitioner's petition under Point V-D of her Opening Brief (Op. Br. pp. 23-24) that there was identification between the certificates on the certificate exchange (e. g., the second exchange) assuming that at the time of the certificate exchange the Great Western certificates represented Dow shares. Respondent's argument under point 2 (Resp's. Br. pp. 18-26) in respect of the certificate exchange appears to be predicated on the assumption that the Great Western certificates did not represent Dow shares at the time of the certificate exchange and on such certificate exchange certificates representing shares in one corporation (apparently, Great Western) were exchanged for certificates representing shares in another corporation (i. e., Dow).

It is respectfully submitted that none of Respondent's arguments can be supported and that accordingly his entire position on this head must fail.

(a) The Great Western shares were individually exchanged for Dow shares by operation of law and the Agreement of Merger.

Both Section 52 of the Michigan General Corporation Act and Section 361 of the California Civil Code direct that the Agreement of Merger shall provide the "manner of *converting* the shares of each of the constituent corporations into shares of the consolidated or merged corporation" (italics supplied).*

Article III of the Agreement of Merger, pursuant to said statutory direction, provides that on the effective date of the merger, each common share of Great Western shall be consti-

*In California Civil Code Section 361 the words "and basis" are added after the word "manner"; the words "each of" are omitted and the word "surviving" is substituted for the word "merged".

cable. Petitioner argued in her Opening Brief that the instant exchange was effected by operation of law but did not claim it was involuntary (Op. Br. pp. 15-22). There is a clear distinction between an exchange by operation of law and an involuntary exchange (*U. S. v. Seattle-First National Bank* (1944) 321 U.S. 583). Accordingly, Respondent's argument in respect of this claimed position of Petitioner is irrelevant.

tuted and converted into one common share of Dow and each preferred share of Great Western shall be constituted and converted into 3/16ths of one common share of Dow. Sections 52 and 53 of the Michigan General Corporation Act and Section 361 of the California Civil Code provide that the Agreement of Merger shall become effective upon the compliance with the statutory requirements of filings, etc. Accordingly, on the effective date of the Agreement of Merger, the Great Western shares were *converted* into Dow shares, as provided in the Agreement of Merger.

U. S. v. Seattle-First National Bank, 321 U.S. 583;
National Supply Co. v. Leland Stanford Jr. University (C.C.A. 9th Circuit, 1943) 134 Fed.(2d) 689;
Copeland v. Minong Mining Co. (1875) 33 Mich. 2;
Ridgway v. Griswold (1878) 20 Fed. Cas. C.C.D. Kansas, Case No. 11819.

See, also, Opening Brief pages 15-20.

Respondent argues that under the statutory provisions above referred to, the individual shares of Great Western were not exchanged for individual shares of Dow and that the provision of Article III of the Statutory Merger, despite its explicit language to the contrary, provides merely for a *rate* of exchange and does not provide that each individual share of the Great Western stock shall be separately converted into or exchanged for a Dow share or fractional Dow share (Resp's. Br. p. 16, footnote 7, p. 17).

This contention is directly contrary to the entire concept of merger law, it being established that on a merger the corporate identity of the merging corporation is merged into that of the surviving corporation and the stock interests in the merging corporation are converted into stock interests in the surviving corporation.

U. S. v. Seattle-First National Bank, supra;
National Supply Co. v. Leland Stanford Jr. University, supra;

Copeland v. Minong Mining Co., supra;
Ridgway v. Griswold, supra.

No word more apt than the word actually used in the statutes and in the Merger Agreement, viz: "convert", could have been used to convey the intention that the individual share-interest or shares in the merging corporation should be changed into individual share-interests or shares of the surviving corporation. Accordingly, since each individual share of the Great Western was converted into a share or fractional share of Dow on the effective date of the statutory merger, it follows that, in effect, such share of Great Western was "exchanged" on such date for the share or fractional share of Dow into which it was converted.

(b) The Federal Courts in applying the Tax Statutes should give effect to the provisions of the merger statutes.

Respondent argues that the instant exchange "is factually essentially the same as other reorganization exchanges *occurring in other states* and must receive the same treatment under the Federal basic statute in order to give the statute uniform application" (italics supplied) (Resp's. Br. p. 16, footnote 7). The implication of this argument is that the merger statutes in question are peculiar to the laws of Michigan and California. Quite the contrary is true, since most states have merger statutes which are substantially identical. Thirty-nine out of the forty-eight states have general merger statutes, and two more have merger statutes applicable only to certain limited classes of corporations. Only seven states have no merger statute at all.

The distinction is not between a statutory merger occurring in *Michigan or California* and a merger occurring in other states, but between a statutory merger, on the one hand, and a reorganization involving a simple transfer of assets from one corporation to another corporation, on the other hand. The United

States Supreme Court in two cases has recognized and given effect to this distinction.

U. S. v. Seattle-First National Bank, supra;
Helvering v. Metropolitan Edison Co. (1939) 306 U.S. 522.
See, also, *National Supply Co. v. Leland Stanford Jr. University, supra.*

For a discussion of the above cases see Opening Brief p. 21.

(c) **The first exchange and second exchange referred to in the Opening Brief are separate transactions. The Great Western certificates from and after the effective date of the merger represented stock interests in Dow.**

Respondent argues (Resp's. Br. p. 17, footnote 8) that the first exchange and second exchange (Op. Br. pp. 11-13) must be regarded as one transaction which was consummated upon the certificate exchange in 1939, and in support of his argument cites cases holding that on a "reorganization" the various integral steps must be regarded as part of one transaction. This argument cannot be sustained. The "plan of reorganization" in the instant case was the statutory merger of Great Western with and into Dow. This took place on or before December 31, 1938. The subsequent 1939 certificate exchange, which took place several weeks later (Record p. 72), was not a part of, and had nothing to do with the statutory merger (see Op. Br. pp. 11-13).

Respondent argues that, while the Great Western stockholders on the effective date of the merger may have acquired an interest in Dow assets, the Great Western certificates did not represent such interest. Clearly this interest was a stock interest, since we have shown the Great Western shares were converted into Dow shares on the effective date of the merger. Since the Great Western certificates immediately prior to the effective date of the merger represented Great Western shares, and on such date the

Great Western shares were converted into Dow shares, it follows that the Great Western certificates thereafter represented such Dow shares.

(d) The identity between the Great Western shares and Dow shares is established by operation of law. The identity between the shares represented by each Great Western certificate after the effective date of the merger and the Great Western share represented thereby immediately prior to such date is clearly established.

Respondent argues that since the business interest represented by the Great Western shares is entirely different from the business interest represented by the Dow shares that the Great Western shares may not be identified with the Dow shares (Resp's. Br. pp. 25-26). The complete answer to Respondent's contention is that such identification is provided by the applicable provisions of the laws of the states of Michigan and California (Secs. 52 and 53 of the Michigan General Corporation Laws and Sec. 361 of the California Civil Code) and the Federal Courts, in applying the Federal Tax statutes, will give effect to such statutory provisions (see supra, pp. 7-8). The situation presented is no different in a case where a corporation acquires an entirely new business. In such case the identity of the shares of the corporation is unaffected. (*Rhode Island Hospital Trust Company v. Doughton* (1926) 270 U.S. 69.)

Respondent further argues that on Petitioner's theory no identity can be established between the individual Great Western shares and the Dow shares for which they were exchanged (Resp's. Br. pp. 26-27). This is not so. There is complete identity established between the Dow shares represented by each Great Western certificate after the effective date of the merger and the Great Western shares represented thereby immediately prior to said date (Op. Br. pp. 16-17).*

*Respondent in other parts of his brief does not appear to have any difficulty in tracing the identification (Resp's. Br. pp. 22-24).

Under this point II we have disposed of every argument of Respondent pertaining to Petitioner's first ground. Accordingly, on this basis alone the decision must be for Petitioner. We will now discuss the arguments urged by Respondent in connection with the second ground.

III.

RESPONDENT'S ATTEMPTED DISTINCTION IN THE MANNER OF THE DETERMINATION, UNDER SECTION 113(a)(6), OF THE BASIS OF STOCK ACQUIRED ON A REORGANIZATION, DEPENDING ON WHETHER THE STOCK WAS ACQUIRED IN EXCHANGE FOR (i) STOCK OF THE SAME CORPORATION, OR (ii) STOCK OF ANOTHER CORPORATION, IS WITHOUT FOUNDATION.

Respondent concedes that under Section 113(a)(6) the basis of stock of one corporation exchanged on a "reorganization" for stock of the same corporation is the same as the basis of the stock for which it is exchanged (Resp's. Br. p. 15). See *Fuller v. Commissioners, supra,* and *Kraus v. Commissioner, supra.*

Respondent argues that the rule of the *Fuller* and *Kraus* cases is not applicable to the instant case since those cases involve exchanges of stock in the same corporation and the instant case involves exchange of stock in one corporation for stock in another corporation, and that, accordingly, the average cost rule is applicable to the instant case and, in support thereof, relies upon the following grounds:

> (a) The average cost rule conforms with the reality of the situation since the Dow shares were acquired at one time and each Dow share acquired had the same value irrespective of the cost of the Great Western shares for which it was exchanged (Resp's. Br. pp. 13-14).
>
> (b) The language of Section 113(a)(6) merely requires that the basis of all the shares received on the exchange shall be the same as the basis of all the shares surrendered on the exchange (Resp's. Br. pp. 17-18).

(c) Petitioner has failed to establish any identity between the certificates surrendered and the certificates received since she has failed to prove an intention to identify (Resp's. Br. pp. 18-24).

The difficulty with Respondent's position is that (i) each of the grounds advanced is applicable equally to the "reorganization" involved in the *Fuller* and *Kraus* cases, i. e., an exchange of stock in the same corporation, and (ii) his arguments fail to give effect to the intended result of the reorganization basis provisions. It is the intention of the reorganization basis provisions that, for the purpose of determining basis of the stock acquired on the reorganization, the acquired stock should "be considered as taking the place of the old property given up in connection with the exchange" (Gregg Statement explaining Sec. 204 of the 1924 Revenue Act).*

A more detailed consideration of each of the grounds advanced by Respondent will show that none of them can be sustained.

(a) The fact that Dow shares were acquired at one time, and are of equal value to one another, is immaterial in connection with the application of Sec. 113(a)(6) and do not support the application of the average cost rule.

Respondent argues that, in view of the fact that the Dow shares were acquired on the statutory merger in exchange for Great Western shares at the same time and are of equal value, that, even though there is identification between the Great Western shares surrendered and the Dow shares acquired, it is proper to apply the average cost rule in determining the basis of the Dow shares acquired, since it conforms to realities of the situation (Resp's. Br. pp. 13-14).

The question here involved is one of statutory construction, viz: the interpretation of the provisions of Section 113(a)(6).

*In connection with the revision of the reorganization provisions by the Revenue Act of 1924, a statement (referred to as the "Gregg Statement") explaining such changes was prepared by Mr. A. W. Gregg, special assistant to the Secretary of the Treasury.

Respondent has failed to show how these factors are relevant in the construction of said section. As a matter of fact, as we shall see, infra, p. 12 to p. 15, these factors are irrelevant in view of the Congressional policy adopted in Section 113(a)(6).

Each of the factors cited by Respondent is applicable to stock of a corporation acquired on a "reorganization" for stock of the same corporation. In such case, the new stock acquired would be acquired at the same time and would have an equal value. Clearly, therefore, these factors do not distinguish the instant case from the *Fuller* and *Kraus* cases involving exchanges, on a reorganization, of stock in the same corporation in which identification is permitted.

(b) Sec. 113(a)(6) directs that, for the purpose of determining basis, the property acquired on a tax-free exchange shall be identified with the specific property for which it was exchanged.

Section 113(a)(6) provides that the basis of the property acquired "shall be the same as in the case of the property exchanged". Respondent argues that the provisions of Section 113(a)(6) "are served when the basis of all the new stock is assigned the basis of all the old stock" (Resp's. Br. pp. 17-18). However, if Section 113(a)(6), as admitted by Respondent, permits identification in the case of stock of one corporation acquired on a reorganization in exchange for stock of the same corporation why does it not likewise permit such identification in the case of stock of one corporation acquired on a "reorganization" for stock of another corporation?

The meaning attributed by Respondent to Section 113(a)(6) cannot be sustained in view of the history and language of the provision and the Congressional policy evidenced thereby. On the contrary, such history, language and Congressional policy indicate that identification for the purposes of determining basis, rather than being prohibited, is directed.

Section 113(a)(6) is derived from Section 202(b) of the Revenue Act of 1918. Section 202(b) provided that "the new stock or securities received [on a tax-free exchange] shall be treated as taking the place of the stock, securities or property exchanged" for the purposes of determining basis. A similar provision was included in Section 202(d)(1) of the Revenue Act of 1921 in a general provision relating to the basis of property acquired on tax-free exchanges.*

In the Revenue Act of 1924 there was a complete revision of the reorganization provisions and the provision in the form now contained in Section 113(a)(6) was included in Section 204(a)(6) of the Revenue Act of 1924. This provision was intended to have the same effect as Section 202(d)(1). See Report of Ways and Means Committee (68th Cong., 1st Sess., H. Rept. 179) p. 16; Report of Senate Finance Committee (68th Cong., 1st Sess., S. Rept. 389) p. 10; Gregg Statement under Section 204.

On pages 16-17 of said Report of Ways and Means Committee, in respect of said section, it is stated: "The general theory of this section is that where no gain or loss is recognized as resulting from the exchange the new property received shall, for the purposes of determining gain or loss from a subsequent sale . . ., be considered as taking the place of the old property given up in connection with the exchange. . . . These provisions are based upon the theory that the types of exchanges specified in Section 203 are merely changes in form and not in substance . . ."†

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*Section 202(d)(1) provided that "the property received shall . . . be treated as taking the place of the property exchanged therefor, . . ."

†See, also, Report of Senate Finance Committee, above cited, pages 10-12, where almost identical language is set forth. The language referred to from both the Ways and Means Committee and Senate Finance Committee Reports appears to be taken from the Gregg Statement in reference to Section 204.

Clearly the Committee Reports are relevant in construing the provisions of Section 113(a)(6) (*Helvering v. Griffiths* [1943] 318 U.S. 371). From these Reports, it is established that Congress intended by Section 113(a)(6) to provide that for the purposes of determining basis the property acquired on a tax-free exchange should be considered as taking the place of the property surrendered on the exchange. Accordingly, it is clear that Congress by Section 113(a)(6) directed that, for the purposes of determining basis, the property acquired on such exchange be identified with the property surrendered on the exchange. Furthermore, the very language of Section 113(a)(6) (viz: that the basis of the property acquired "shall be the same *as in the case* of the property exchanged" [italics supplied]) likewise directs that identification shall be made. This is no mere argument, as claimed by Respondent, that the sum of the bases of the various units of property acquired shall equal the sum of the bases of the various units of property surrendered. In view of the foregoing, it is clear that Section 113(a)(6) rather than permitting, as contended by Respondent, the application of the average cost rule, instead directs identification between the property acquired and the property exchanged for the purpose of determining the basis of the property acquired.

In view of the Congressional policy adopted in Section 113(a)(6), it is clear that the factors cited by Respondent (see supra, pp. 11-12) in supporting the application of the average cost rule (i. e., that the Dow shares were acquired at one time and have an equal value) are irrelevant since Congress has directed that the Dow shares acquired, for the purposes of determining basis, should be treated as though they were the Great Western shares exchanged.

(c) Identification between the Great Western certificates surrendered and the Dow certificates acquired has been clearly established. Identification is a matter of fact and intention is irrelevant.

Respondent argues that no identification has been established between the Great Western certificates surrendered and the Dow

certificates received, and that the finding by the Tax Court of identification between the Dow shares and Great Western shares may not be supported. He states that any such identification is entirely arbitrary, and further argues that no intention to identify the Great Western certificates surrendered with the Dow certificates received has been established excepting the act of the Transfer Agent (Resp's. Br. pp. 18-22, p. 24, footnote 9). It is respectfully submitted that the facts as stipulated support the Tax Court's finding of identification (Record p. 22).

In support of this argument, Respondent refers to the case of *Crespi v. Commissioner* (C.C.A. 5th, 1942) 126 Fed.2nd 699. In this case the charter of a corporation expired by operation of law and its assets passed to its officers and directors as trustees for the stockholders. The property was transferred to a new corporation which issued shares to taxpayer representing his interest in the property. Taxpayer endeavored to treat the transaction as an exchange of stock of the old corporation for stock in the new corporation. The court held (126 Fed.2nd 699, 701) "each share represented an aliquot part of this value [the value of the property transferred], and therefore each took the same basis as every other share." The *Crespi* case, therefore, involved an exchange of property for stock and not an exchange of stock for stock and its holding is entirely immaterial to the instant case.

Respondent argues at length, without the citation of any authority whatsoever, that identification is a matter of intention. On the contrary, it is well established by the decisions that identification is a matter of fact and intention has no relevance whatsoever in establishing identification. In the instant case it is clear from the stipulation that certain identifiable Dow certificates were issued in lieu of certain identifiable Great Western certificates (Record p. 22). Identification, therefore, as a matter of fact, between the Dow certificates acquired and the Great Western certificates surrendered, has been established. It is immaterial whether Petitioner had any foreknowledge of the specific

Dow certificates which were to be issued in lieu of the specific Great Western certificates. If, for example, a taxpayer sells certain identifiable shares but intended and directed that other shares be sold, nevertheless, for the purpose of determining gain or loss on the sale, the basis of the property sold is taken to be the basis of the property *actually sold* and not that of the property *intended* to be sold.

> *Davidson v. Commissioner* (1938) 305 U.S. 44;
> *Smith v. Higgins* (C.C.A. 2nd, 1939) 102 Fed.2nd 456;
> *Commissioner v. Merchants & Manufacturers Fire Insurance Company* (C.C.A. 3rd, 1934) 72 Fed.2nd 408;
> *Holmes v. Commissioner* (C.C.A. 3rd, 1943) 134 Fed. 2nd 219.

Furthermore, the identification between the Dow certificates issued and the Great Western certificates surrendered is the same as the identification which is established when a taxpayer receives from a corporation new certificates for old certificates. It is clear that identification may be established in such case (*James W. Arrott, Jr. v. Commissioner* [1936] 34 B.T.A. 133). Compare *Fuller v. Commissioner, supra,* where identification was permitted, in determining the basis of stock issued on a stock split-up, between the new split-up stock and the original stock. It follows from what has been said that the question of intention is immaterial in establishing identification where, as here, identification has been established as a matter of fact. The identification in the *Fuller* case is the same as in the instant case, i. e., through action of the stock transfer agent and Respondent's attempt (Resp's. Br. pp. 27-28) to distinguish the *Fuller* case is without merit.

Respondent argues that in the case of the Dow certificates issued for the Great Western preferred certificates complete identification has not been established (Resp's. Br. pp. 23-25). In the case of such shares, Dow certificates representing 162-3/16 common shares were issued as a unit for the Great Western cer-

tificates representing 865 preferred shares (Record p. 32). 162 shares of said 162-3/16 shares were sold in the transaction involved in the instant case. Clearly the Dow certificates representing said 162-3/16 shares have been identified with the Great Western preferred certificates.

Cf. *James W. Arrott, Jr. v. Commissioner supra;*
Bancitaly Corporation v. Commissioner (1936) 34 B.T.A. 494;
Melcher v. U. S., U. S. Court of Claims 1937, 19 Fed. Supp. 663.

Since said 162-3/16 Dow shares were issued as a unit for the Great Western preferred shares, it was necessary, since only part of the shares were sold in the involved transaction, to use some arbitrary method for determining basis of such shares such as the "first-in first-out" rule or the average cost rule. Petitioner in view of the rule of *Commissioner v. Von Guten* (C.C.A. 6, 1935) 76 Fed.(2d) 760, for the purposes of determining gain or loss on the sale on the portion of said 162-3/16 Dow shares sold in the instant transaction, applied the average cost rule by dividing the aggregate cost or other basis of the Great Western preferred shares by 162-3/16 and multiplying the result by 162, the number of shares sold.

Respondent claims that this results in the adoption of a hybrid rule and that, accordingly, the average cost rule should be used for all the Dow shares acquired (Resp's. Br. pp. 24-25). The same identical situation arises where a taxpayer, in one transaction, sells certain identifiable stock and also part of a block of stock. In such case it is well established that the basis of the identifiable stock is used and that the basis of portion of the block of stock sold is determined on the "first-in first-out" rule by reference to said block of stock.

Arrott v. Commissioner, supra;
Bancitaly Corporation v. Commissioner, supra;
Melcher v. U. S., supra;
G.C.M., 8426, IX-2, Cumulative Bulletin, p. 92.

It is submitted that each argument advanced by Petitioner in support of his contention that identification cannot be used in the instant case has been fully answered.

IV.

CONCLUSION

In view of the foregoing, it is respectfully submitted that the decision of the Tax Court should be reversed.

Respectfully submitted,

W. H. ORRICK,
CHARLES L. BARNARD,
Attorneys for Petitioner

ORRICK, DAHLQUIST, NEFF,
BROWN & HERRINGTON,
Of Counsel